

SBRA CASE HYPOTHETICAL

On July 27, 2020 Starbrew Coffee, a small, local chain of coffee shops located throughout the Philadelphia suburbs, through its pre-bankruptcy counsel ABC Law Firm, filed for bankruptcy in the District of Delaware. Starbrew's business model includes training world class baristas at its location, essentially making Starbrew a coffee shop and coffee school all in one. Starbrew still has its storefronts, but furloughed employees during the summer as it struggled to safely re-open its locations during the pandemic, allowing its employees to benefit from CARES Act unemployment benefits. At the time of filing, Starbrew, a Delaware corporation wholly owned by Robyn Fenty ("Fenty"), had \$4.4 million of debt, including \$8,200 owed to ABC Law Firm as of the petition date. It fully intends to resume business operations once locations have been modified to ensure social distancing and safety have been made. Starbrew elects for a Chapter 11 Subchapter V bankruptcy when filing for bankruptcy. 70% of Starbrew debts stem from normal operating expenses, creditors include coffee vendors in Latin America, a local bakery that provides fresh baked goods to coffee shops, landlords of various storefronts, its normal attorney, merchandise suppliers, and its insurance carriers. Included in the business debt is a \$2.1 million unsecured business loan made to Starbrew by Creditor Bank (Starbrew largest creditor) that Ms. Fenty personally guaranteed. Additionally, in addition to granting the personal guarantee, five years before the bankruptcy, Ms. Fenty took a second mortgage in the amount of \$50,000 on her residence, the proceeds of which was loaned to Starbrew for its operations under a promissory note.

On the petition date, Starbrew filed a motion for debtor-in-possession financing whereby Ms. Fenty offered to provide it with \$100,000 in superpriority DIP financing. Under the terms of the DIP, Starbrew is required to acknowledge the validity of the loan from Fenty and make representation in the DIP Order that the loan is secured by a lien on all of Starbrew's assets. In addition to the representations, the proposed DIP financing order purports to grant Fenty a lien on avoidance action, a 506(c) waiver, and to make the order (upon entry by the court) binding on all creditors as well as any future trustee. No documents were filed with the motion supporting validity or security of Fenty's loan.

Starbrew also sought authorization from the Court to apply for a PPP loan under the Consolidated Appropriations Act, 2021 ("CARES Act II") signed into law by President Trump on

December 27, 2020 (the “Second Stimulus Bill”), which was loan was obtained by Starbrew in the amount of \$100,000.

On August 1, 2020, the notice of the First Meeting of Creditors was filed by the United States Trustee on the court's docket setting September 9, 2020 as the deadline for the filing of all non-governmental proofs of claim (“341 Notice”). Conspicuously missing, however, was the deadline for the filing of governmental proofs of claim that is routinely contained within a 341 Notice. Two weeks before its plan was due to be filed, Starbrew filed an expedited motion seeking to extend the 90-day deadline on the theory that it needed the court to first fix a deadline for governmental entities to file proofs of claim as it did not make sense for it to file a plan of reorganization where the IRS, and certain state and local governments who had tax claims had not yet filed proofs of claim and were each scheduled as contingent claims. A hearing was set on the motion to determine if Starbrew should not justly be held accountable for failing to file a plan.

Confirmation Scenario A (Consensual Plan Confirmation): With the help of the Subchapter V Trustee, Starbrew was able to get its main creditor, Creditor Bank, on board with the terms of Starbrew's proposed plan and because no creditor objected to the plan, a consensual plan was confirmed, as required by §1191(a). The plan also met the §1191(c)(2) requirement that all of Starbrew's disposable income in the next three (3) years will go towards funding the plan. This will not include reserves stored for expected capital expenditures necessary for the normal course of business, like the planned addition of state-of-the-art on-site espresso roasting machines at all of its locations. The plan provides that the trustee does not need to make the payments. Starbrew moved to terminate the trustee's services under §1183(c)(1). Administrative expenses, including the cost of the trustee and professionals hired by Starbrew, were also allowed per §503(b)(2).

One issue that arose during the proceedings was Starbrew's ability to make all payments, as required by §1191(c)(3)(A), during the plan. Starbrew's financial projections for the plan utilize projections from normal business operations, pre-March 2020. It is unclear how different these projections are moving forward as the COVID-19 pandemic progresses. The plan included the required §1191(c)(3)(B) remedies in case Starbrew did not make all of the required payments, so it was allowed. The court can also allow a plan modification under §1193(b) if it is deemed appropriate because of the business conditions created by the pandemic.

Confirmation Scenario B (Non-Consensual Plan Confirmation): Creditor Bank, the largest non-insider creditor rejected the plan, thus, requiring the plan to be confirmed per the cramdown provisions under §1191(b).

In its objection to confirmation, Creditor Bank alleges that the plan was not confirmable because it did not comply with section 1129(7) as creditors would receive less than they are entitled to if Starbrew was liquidated. The Liquidation Analysis presented by Starbrew allegedly did not include any support for the sale value asserted by the Debtor and it assumed Fenty's prepetition loan would be treated as a secured claim entitle to payment before unsecured creditors. It also did not include an analysis of avoidance claims that may exist against Fenty notwithstanding that Fenty received over \$100,000 in distribution in the 90 days leading up to the filing of the bankruptcy. In addition, Creditor Bank asserts that the 3-year plan period was insufficient given that creditors would receive approximately 20% on the value of their claims if Starbrew's projections are correct, and as such, Creditor Bank asserts that a 5-year plan period should be ordered. Creditor Bank also argues that the Subchapter V Trustee not Starbrew should be making the distributions under the plan. Starbrew's counsel pointed out that allowing the Debtor to make the payments would result in significant savings as no fees would have to be paid to the Trustee and that the court has already confirmed a non-consensual plan with the exact same provision.

Other Potential Case Scenarios:

1. Creditor Bank has indicated that it will enforce the personal guarantee against Ms. Fenty if its debt is not paid in full by Starbrew. Ms. Fenty has engaged personal bankruptcy counsel and is contemplating a personal bankruptcy filing. If she also files under Subchapter V of chapter 11, how will the cases proceed? Will they be jointly administered or consolidated? Can the lien on Ms. Fenty's home that is business debt be stripped off?
2. Assume Creditor Bank instead of being unsecured has a lien on all of the Debtor's assets and objects to the valuation of the Debtor's assets as set out in the plan. Based on the valuation Creditor Bank is undersecured and thus, the Debtor's plan proposes to bifurcate Creditor Bank's claim into secured and unsecured debt. The plan proposes to pay the secured claim in full over the term of the plan and Creditor Bank would get a 20% distribution on account of the unsecured portion of the claim under the plan. Creditor Bank objects to the plan, and in particular the valuation of the assets. What are the debtor's rights as a result and what if anything can Creditor Bank do to prevent confirmation?